

§ 1.723-1

contributed property is subject to indebtedness or if liabilities of the partner are assumed by the partnership, the basis of the contributing partner's interest shall be reduced by the portion of the indebtedness assumed by the other partners, since the partnership's assumption of his indebtedness is treated as a distribution of money to the partner. Conversely, the assumption by the other partners of a portion of the contributor's indebtedness is treated as a contribution of money by them. See section 752 and § 1.752-1. The provisions of this section may be illustrated by the following examples:

Example 1. A acquired a 20-percent interest in a partnership by contributing property. At the time of A's contribution, the property had a fair market value of \$10,000, an adjusted basis to A of \$4,000, and was subject to a mortgage of \$2,000. Payment of the mortgage was assumed by the partnership. The basis of A's interest in the partnership is \$2,400, computed as follows:

Adjusted basis to A of property contributed	\$4,000
Less portion of mortgage assumed by other partners which must be treated as a distribution (80 percent of \$2,000)	1,600
Basis of A's interest	2,400

Example 2. If, in example 1 of this section, the property contributed by A was subject to a mortgage of \$6,000, the basis of A's interest would be zero, computed as follows:

Adjusted basis to A of property contributed	\$4,000
Less portion of mortgage assumed by other partners which must be treated as a distribution (80 percent of \$6,000)	4,800
	(800)

Since A's basis cannot be less than zero, the \$800 in excess of basis, which is considered as a distribution of money under section 752(b), is treated as capital gain from the sale or exchange or a partnership interest. See section 731(a).

§ 1.723-1 Basis of property contributed to partnership.

The basis to the partnership of property contributed to it by a partner is the adjusted basis of such property to the contributing partner at the time of the contribution. Since such property has the same basis in the hands of the partnership as it had in the hands of the contributing partner, the holding period of such property for the partnership includes the period during which it was held by the partner. See section 1223(2). For elective adjustments to the

26 CFR Ch. I (4-1-03 Edition)

basis of partnership property arising from distributions or transfers of partnership interests, see sections 732(d), 734(b), and 743(b).

DISTRIBUTIONS BY A PARTNERSHIP

§ 1.731-1 Extent of recognition of gain or loss on distribution.

(a) *Recognition of gain or loss to partner*—(1) *Recognition of gain.* (i) Where money is distributed by a partnership to a partner, no gain shall be recognized to the partner except to the extent that the amount of money distributed exceeds the adjusted basis of the partner's interest in the partnership immediately before the distribution. This rule is applicable both to current distributions (i.e., distributions other than in liquidation of an entire interest) and to distributions in liquidation of a partner's entire interest in a partnership. Thus, if a partner with a basis for his interest of \$10,000 receives a distribution of cash of \$8,000 and property with a fair market value of \$3,000, no gain is recognized to him. If \$11,000 cash were distributed, gain would be recognized to the extent of \$1,000. No gain shall be recognized to a distributee partner with respect to a distribution of property (other than money) until he sells or otherwise disposes of such property, except to the extent otherwise provided by section 736 (relating to payments to a retiring partner or a deceased partner's successor in interest) and section 751 (relating to unrealized receivables and inventory items). See section 731(c) and paragraph (c) of this section.

(ii) For the purposes of sections 731 and 705, advances or drawings of money or property against a partner's distributive share of income shall be treated as current distributions made on the last day of the partnership taxable year with respect to such partner.

(2) *Recognition of loss.* Loss is recognized to a partner only upon liquidation of his entire interest in the partnership, and only if the property distributed to him consists solely of money, unrealized receivables (as defined in section 751(c)), and inventory items (as defined in section 751(d)(2)). The term *liquidation of a partner's interest*, as defined in section 761(d), is the